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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45

AT&T OPPOSITION TO PETITIONS FOR RECONSIDERATION

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SUMMARY

AT&T shows in Part I that, contrary to the position of some parties, the Commission's decision in the May 8, 1997 Universal Service Order to limit federal universal service support for high cost areas served by nonrural incumbent local exchange carriers to 25% of the difference between the forward-looking economic cost of providing the supported service and a nationwide revenue benchmark, is reasonable. The Act requires that together Federal and State universal service support must be sufficient, and there is no reason to believe that with a Federal-State partnership, it will not be. Given the strong opposition of some states to assessment of intrastate revenues for the high cost/low-income programs, the Joint Board recommendation that the contribution base issue should be examined in the context of the forthcoming proxy model proceeding, and the FCC's commitment to continue to work with the States to ensure the necessary funding, the Commission's decision, which promotes comity, is sound. At the same time, AT&T agrees that a unified national fund in which intrastate revenues are included in both the assessment and recovery base would have substantial benefits, including avoiding any undue burdens on high cost, low population states.

As demonstrated in Part II, rural ILEC challenges to the high cost support program, which provides a three-year transition during which embedded cost subsidies will remain

available, are baseless. Even if a rural company's rate-of-return fell below 11.25 percent, that would not necessarily constitute a "taking." Competitive neutrality requires that a new entrant that wins the customer receive the same embedded subsidy level as the rural incumbent. As in the past, LTS support should be available to NECA pool members and, to ensure competitive neutrality, to new entrants competing with them. Contrary to some parties' contentions, the indexed cap on the former high cost fund component of the USF should be retained to "prevent excessive growth in the size of the fund during the period preceding the implementation of forward-looking mechanisms." Limiting the amount of corporate operations expense for USF subsidy purposes is reasonable given that this expense results from managerial priorities that are not directly related to the provision of universal service. Limiting USF support for exchanges sold after May 7, 1997 is reasonable because it avoids the higher embedded subsidies available to rural ILECs from becoming a factor in acquiring exchanges.

As AT&T shows in Part III, the Commission should change the mechanism for universal service support recovery to a competitively neutral mandatory end user surcharge on all interstate retail telecommunications service revenues. As MCI and Comcast/Vanguard confirm, the current recovery mechanism is not competitively neutral because while ILECs can recover their USF assessment through "wholesale" access charges, competitive carriers, including carriers entering the local market through total service resale and CMRS providers, will have no ability to deflect USF recovery through access charges, placing them at a serious competitive disadvantage *vis-à-vis* the incumbent. Moreover, a mandatory end user surcharge would moot issues regarding the impact of the X-Factor on ILEC USF recovery, allegations by end users that a permissive pass-through of USF support obligations abrogates fixed-price contracts, and it would obviate the need for access and end user rate fluctuations as carriers' support obligations change.

In Part IV, AT&T demonstrates that the Commission's construction of Section 214(e) as to certification of eligible carriers is correct and the Commission need not clarify at this juncture whether its pronouncements are "instructive rather than binding," as some states request. Moreover, the suggestion by a few parties that UNE users do not meet the "own facilities" requirement is incorrect. Because a carrier using UNEs has obtained the exclusive use of the facility and compensates the ILEC for the forward-looking economic cost, to the extent that the cost of serving the customer exceeds that level, it is the UNE purchaser who is entitled to USF support.

In Part V, AT&T shows that, contrary to the positions of paging firms, systems integrators and satellite providers, the Commission's ruling that they are all subject to universal service support when providing interstate telecommunications services for a fee is correct. The Commission's holding ensures the broad contribution base needed to sustain universal service support. If the Commission were to exempt private carriage providers, it would be skewing business decisions and would be creating a huge loophole whereby telecommunications service providers could serve their largest business customers on a private carriage basis without USF obligations, thereby seriously eroding the foundation for universal service support.

In Part VI, AT&T shows that resellers will be able to receive Lifeline support either by purchasing a discounted Lifeline service from the ILEC or by purchasing a discounted basic local exchange service and applying to the USF Administrator for the Lifeline subsidy when providing service to a Lifeline eligible customer. In the latter instance, as Kansas correctly notes, the Commission should consider exempting resellers from Section 214(e) certification requirements. AT&T agrees with USTA's and U S WEST's suggestion that carriers should be permitted to offer <u>either</u> toll blocking <u>or</u> toll control to Lifeline customers, given the enormous burdens associated with the latter. AT&T suggests that carriers not be required to pay a PICC for a Lifeline customer who has elected toll blocking because the customer has indicated that it will not be placing long distance calls. AT&T has no objection to USCC's suggestion that the PICC be waived for Lifeline customers who do not presubscribe to an IXC because recovery of the charge from the customer could provide incentives not to elect toll blocking.

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Federal-State Joint Board on Universal Service	CC Docket No. 96-45

AT&T OPPOSITION TO PETITIONS FOR RECONSIDERATION

Pursuant to Section 1.429 of the Commission's Rules, 47 C.F.R. § 1.429, and its Public Notice, FCC Report No. 2212, published in the Federal Register on August 1, 1997 (62 Fed. Reg. 41386), AT&T Corp. ("AT&T") hereby responds to other parties' petitions for reconsideration and/or clarification of certain rulings in the May 8, 1997 Universal Service Order.[1] By separate pleading filed today, AT&T responds to petitions for reconsideration of the May 16, 1997 Access Reform Order.[2]

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[1] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Report and Order, FCC 97-157, released May 8, 1997, and published in the Federal Register on June 17, 1997 (62 Fed. Reg. 32862), pets. for review pending sub nom. Texas Office of Public Utility Counsel v. FCC, Nos. 97-60421 *et al.* (5th Cir.) ("Universal Service Order"), id., Order on Reconsideration, FCC 97-246, released July 10, 1997; Second Order on Reconsideration, FCC 97-253, released July 18, 1997. Unless another Order is specifically referenced, all paragraph citations herein are to the Universal Service Order. Appendix A lists the parties filing petitions and the abbreviations used to identify them herein.

[2] Access Charge Reform, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, First Report and Order, FCC 97-158, released May 16, 1997, and published in the Federal Register on June 11, 1997 (62 Fed. Reg. 31868) pets. for review pending sub nom. Southwestern Bell Tel. Co. v. FCC, Nos. 97-2618 *et al.* (8th Cir.) ("Access Reform Order"), id., Order on Reconsideration, FCC 97-247, released July 10, 1997.

I. ALTHOUGH THE COMMISSION'S APPROACH IS REASONABLE, IF THE COMMISSION ADOPTS A UNIFIED FEDERAL UNIVERSAL SERVICE FUND, IT SHOULD INCLUDE BOTH INTERSTATE AND INTRASTATE REVENUES IN BOTH THE ASSESSMENT AND RECOVERY BASE OF THE HIGH COST AND LOW-INCOME PROGRAMS.

A number of parties challenge the Commission's decision to limit federal universal service fund ("USF") support for rural, insular and high cost areas served by nonrural incumbent local exchange carriers ("ILECs") to 25% of the difference between the forward-looking economic cost ("FLEC") of providing the supported service and a nationwide revenue benchmark, while relegating the remaining 75% funding to the States.[3] They contend that the 25% funding level does not meet Section 254(b)(1) of the 1996 Telecommunications Act's requirement that support be "specific, predictable and sufficient" (Wyoming at 2), and this limitation discriminates against consumers in states with high costs and low population who will have to pay more per capita to fund the 75% residual, thereby violating that Section 254(b)(3)'s "reasonable comparability of rates" requirement. Vermont at 1, 6; Wyoming at 2.

Section 254(b)(3) provides that together Federal <u>and</u> State universal service support mechanisms must be sufficient

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[3] Alaska at 6, 8; ATA at 1; Arkansas at 1. Parties have raised similar claims with respect to high cost support for rural companies, which will gradually shift to USF support based on forward-looking economic cost, commencing no sooner than January 1, 2001 (para. 204). RTC at 3; United at 4; Western Alliance at 14. Issues related to rural telephone companies are addressed in Part II.

to preserve and advance universal service (paras. 3, 7). AT&T believes that, given the strong objection of some states to assessment of intrastate revenues for purposes of federal high cost universal service support (Pennsylvania at 2) and lack of a Joint Board recommendation to assess intrastate revenues, it was not unreasonable for the Commission to elect to proceed in the manner that it did, *i.e.*, to limit federal funding to the 25% level, which reflects the interstate assignment of loop costs (without factoring in any additional interstate assignment of high cost loops) and leaving the states to address the issue of how high costs will be recovered within their jurisdictions (paras. 201, 223, 268-269, 833).

Indeed, the Commission expressly declined "to exercise the full extent of [its authority which it found includes the right to assess intrastate revenues for high cost support[4]] out of respect for the states and the Joint Board's expertise in protecting universal service" (para. 817). While promoting federal/state comity (para. 824, 831), the Commission reaffirmed its belief that the "states will continue to participate fully in this federal-state partnership and that the contributions collected by both jurisdictions will be sufficient" (para. 831). The Commission stated its intent to "seek additional factfinding and deliberation by the Joint Board, and further coordination with individual state commissions, during approximately the next fifteen months"

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[4] See paras. 807, 813.

(paras. 3, 203). At the same time, the FCC indicated that it would "continue to work with the Joint Board on this issue to develop a unified approach to the low-income and high cost mechanisms. . . ." (para. 808).[5]

Not only is the Commission's approach sensible, but it is also consistent with the Joint Board's recommendation that "the question of interstate/intrastate contribution should be coordinated with the issues of appropriate forward-looking mechanisms and appropriate revenue benchmarks" (para. 832), an issue which still remains to be addressed by the Commission (paras. 206, 248). Moreover, the Commission made a commitment to closely monitor universal service issues, pointing out that, as the states convert their own support programs into explicit mechanisms, it "will be able to assess whether any additional support is necessary to ensure that quality services remain 'available at just, reasonable and affordable rates'" (para.

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[5] Unless and until a unified approach is adopted, carriers will have to allocate their revenues between state and interstate jurisdictions for purposes of making universal service contributions. Although determining the jurisdiction of a landline call is relatively easy, the same is not true for calls made on wireless networks. Commercial mobile radio services ("CMRS") customers do not make or receive calls from a fixed location, and often a call can begin as an intrastate call and end as an interstate call as the subscriber moves about. Accordingly, AT&T agrees with AirTouch (at 10-12) and CTIA (at 20-23) that the Commission should allow CMRS providers to use the procedures developed for allocating revenues they report for the Telecommunications Relay Service program in calculating the revenue they must report for universal service contributions. This approach has the benefit of offering CMRS carriers the flexibility they need to make universal service compliance workable as well as a reliable method to track traffic.

834, citing Section 254(b)(1)). Thus, by no means has the Commission abandoned its vigilant safeguarding of universal service.

Notwithstanding the reasonableness of the Commission's decisions on this issue, as AT&T has previously indicated in this proceeding, a national fund, assessed and recovered from both interstate and intrastate retail revenues, has substantial advantages.[6] Thus, AT&T does not disagree with Sprint's observation (at 2) that universal service is a "national issue requiring a national solution." And, AT&T would welcome "a combined state and federal USF plan that provides a reasonable level of support to intrastate as well as interstate services." Id. This approach would recognize, as U S WEST (at 3) points out, that "[a]t bottom, providing high cost service involves making transfers from customers who can be served at low cost to those who can be served only at high cost." A unified fund would recognize that ubiquitous service benefits all consumers nationwide. U S WEST at 5. Combined use of interstate and intrastate retail revenues would provide a sufficient funding base so that states with disproportionately high costs will not be unduly burdened. It would also mean that potentially difficult questions of the jurisdictional identity of revenues would be avoided and that

[6] See AT&T Comments, CC Docket No. 96-45, filed April 12, 1996, at 8-9; id., AT&T Further Comments, filed August 2, 1996, at 18-19, 23; AT&T Comments, filed December 19, 1996, at 4-9; AT&T Reply Comments, filed January 10, 1997, at 3-8.

all carriers would contribute and that no carrier could "game" the process to avoid USF assessments. U S WEST at 7.

Should the Commission adopt a unified national fund approach either on reconsideration or in the future, to ensure that all providers contribute in an equitable manner, the federal USF should be extended to fund 100% of the difference between the forward-looking economic cost of the supported service and the nationwide benchmark only if intrastate retail revenues are included in both the assessment and recovery base of the fund. This will prevent interstate services from being disproportionately burdened with USF support obligations. Moreover, any support received from a unified fund should be used to reduce access charges at the federal and state levels.

As an alternative to such a unified national fund, the Commission may invite states to assess interstate retail revenues billed in the state, along with intrastate revenues, to support explicit funding of the state responsibility for 75% of the difference between the forward-looking economic cost of providing the supported service and a nationwide revenue benchmark, provided that the state reduces access charges in that state.[7] AT&T would have no objection to such an

7 Assuming these conditions are met, AT&T disagrees with MCI's position (at 6) that states should not be permitted to assess interstate and international revenues for their state USF funds because the federal fund does not include intrastate revenues in the high cost fund assessment and recovery base. On the other hand, as MCI points out (at 4), because the federal fund makes implicit interstate support explicit, the Commission correctly determined that USF support received by a carrier from the federal fund must be

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arrangement in return for corresponding offsets against access (state or interstate) charges. Enlarging the assessment and recovery base for state USF funds to include interstate revenues billed in the state should ameliorate the impact of a smaller federal fund on any given state.[8]

However, and contrary to the positions of some parties (Sprint at 2; USTA at 9; Vermont at 5; Wyoming at 3), if the Commission does not opt for a "unified national fund," it should not extend any transitional interstate assignment of high loop costs because: (1) it would be a continuation of the embedded cost methodology beyond the January 1, 1999 cutover to forward-looking economic cost for nonrural ILECs (para. 209), and (2) it will duplicate part of the high cost loops that will be reflected in the proxy model methodology. Accordingly, contrary to USTA's request, there should be no further offset to interstate access reductions to reflect additional high loop costs for these companies.[9]

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removed from interstate access charges. Access Reform Order, para. 381.

8 The Commission should also consider allowing states to opt to have the Administrator of the federal USF implement the explicit state funds for the 75% differential, including having the national fund bear the administrative costs. This would provide an extra incentive for states to choose this alternative.

9 Under the Access Reform Order (para. 381), ILECs must use any USF support from the federal fund to satisfy the interstate revenue requirement otherwise collected through interstate access charges.

II. THE COMMISSION SHOULD NOT MODIFY THE USF APPROACH IT ADOPTED FOR RURAL ILECS.

In light of the special circumstances faced by small incumbent rural ILECs, the Commission determined that they should continue to receive USF support for a three-year transition period based on embedded cost, with only minor modifications to the existing High Cost Fund ("HCF") loop support (paras. 300-301), DEM Weighting (paras. 303-304), and Long Term Support ("LTS") (paras. 305-306) programs. The Commission also limited the amount of corporate operations expense that could be recovered from the USF (paras. 283, 307); capped the amount of USF support available for newly acquired exchanges (paras. 307-308); and continued the existing indexed cap on the high cost fund (para. 302). Only after this transition, and commencing no sooner than January 1, 2001, would rural ILECs begin to receive USF support based on forward-looking economic cost (paras. 291-294).

Consistent with the requirements of Sections 214(e) and 254 that any qualifying carrier be eligible to receive universal service support, the Commission required that HCF, DEM Weighting and LTS be recovered from the new USF, rather than access charges, and that the subsidy be portable commencing January 1, 1998, with an eligible new entrant receiving the same level of support as the rural incumbent, if the new entrant wins the customer (paras. 311-315).

Rural companies challenge virtually every aspect of the FCC's rulings. As shown below, their contentions are without merit and should be rejected.

RTC (at 1-5) and Rural Tel (at ii, 1-9) contend that the Commission's decision limiting federal USF support to 25% of the difference between the forward-looking economic cost of the supported service and a nationwide revenue benchmark, coupled with an inability to recover booked costs, will result in an unconstitutional "taking" of their property and is arbitrary and capricious. As demonstrated in Part I above, given the reluctance of some states to participate in a unified USF, the Commission's decision to limit federal funding was reasonable and should not jeopardize universal service. The states' position also suggests that, to the extent a legitimate "takings" concern were to arise, it is not the Commission's decision that should be considered the cause.

In all events, Rural Tel is wrong in claiming that an unconstitutional taking would result if its rate-of-return dropped below 11.25 percent. Both the 1996 Act and case law permit the Commission to base cost recovery decisions on the "actual present value" of assets employed in providing service. Duquesne Light Co. v. Barasch, 488 U.S. 299, 308 (1989); Market St. Ry. Co. v. Railroad Comm'n of California, 324 U.S. 548, 564-67 (1945). Therefore, the failure of a firm to recover all of its historical costs or to achieve its authorized rate-of-return, which was based on those costs, does not necessarily constitute a taking.[10] Nonetheless, the Commission has

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[10] A taking does not occur unless a firm could show that the "overall impact of the rate order[] . . . jeopardize[s] the financial integrity of the compan[y], either by leaving [it]

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indicated that it will consider issues relating to ILEC recovery of historical costs in a separate proceeding (Access Reform Order, para. 14), and questions concerning what recovery, if any, an ILEC should be provided should be addressed in that context, not here.

Rural Tel (at 7) also complains that the new regime under which per-line USF support and recovery of local switching costs via DEM Weighting become portable further undermines the ability of rural firms to recover their embedded costs during the transition to FLEC-based support because it allows the new entrant to take that support away from the incumbent.[11] Basically, it contends that support for competitive local exchange carriers ("CLECs") should not be measured by the same methodology as for the incumbent. But, as the Commission correctly found (para. 313), calculating support based on the same economic standard for incumbents and new

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insufficient operating capital or impeding [its] ability to raise future capital." Duquesne Light Co., 488 U.S. at 312. None of the rural ILECs has attempted to make this showing. Rather, the evidence they have presented is based on historical cost, which cannot establish a taking.

[11] Contrary to Rural Tel's assertion (at 7-8, 12-15), there is nothing arbitrary about the Commission's decision (para. 212) to treat DEM Weighting as an explicit subsidy to be recovered from the USF rather than access charges. DEM Weighting payments embedded in access charges are designed to ensure affordability of local service by permitting rural LECs to recover more of their switching costs from access and less from local rates. Section 254(d) requires that all such subsidies be recovered from all providers of interstate telecommunications service, not just IXCs. Shifting DEM Weighting recovery to the USF accomplishes that result.

entrants is necessary to ensure competitive neutrality. Thus, the fact that a CLEC would receive USF support in a rural company area for an interim period based on embedded cost is a direct result of the transition program that the Commission has afforded to rural ILECs.

RTC (at 9) contends that LTS payments should be limited to members of the NECA common line pool and not be portable, whereas ALLTEL (at 2-4) and USTA (at 12) maintain that LTS payments from the USF should be available to all rural LECs irrespective of NECA common line pool membership. The Commission should reject each of these contentions. As the Commission properly explained (para. 213), LTS support payments were designed to permit carriers with higher than average loop costs that are NECA pool members to charge a nationwide average interstate CCL access rate. Contrary to RTC's position, as a subsidy program, LTS must be portable and made available to any eligible CLEC that competes with a NECA pool member to ensure competitive neutrality. At the same time and consistent with the original premise of the LTS program, LTS support should <u>not</u> be extended to rural ILECs that have opted to leave the NECA pool.[12] Indeed, if an ILEC leaves the NECA pool and loses its LTS support, to ensure competitive neutrality, that support

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[12] If an ILEC chooses to leave the NECA pool, it is likely due to achieved efficiencies whereby it has become more of a "contributor" to the NECA "pooled" revenue requirement than a "receiver." When an ILEC leaves the pool, it does so with full knowledge that it will no longer be entitled to receive LTS.

should likewise be withdrawn from any CLEC receiving LTS support in that ILEC's territory.

USTA (at 16-17) argues that because of the inclusion of new elements (such as DEM Weighting and LTS) in the USF, a capped fund may not ensure full recovery of the traditional HCF loop subsidies plus DEM and LTS, and, along with Western Alliance (at 11), urges that the cap on the USF be eliminated. AT&T believes that the HCF indexed cap applies only to the high cost loop component of the USF -- the only aspect previously subject to an indexed cap -- (paras. 273, 300-302 and Appendix I, Section 36.601(c)), and that LTS support (paras. 305-306 and Appendix I, Section 54.303) and DEM Weighting (paras. 303-304 and Appendix I, Section 54.301) will be permitted to grow based on the FCC-specified formulas, independent of the indexed cap on the HCF component.

At the same time, and contrary to RTC's suggestion (at 18), the Commission prudently decided (para. 302) to continue the indexed cap on the HCF component of the USF, to "prevent excessive growth in the size of the fund during the period preceding the implementation of forward-looking mechanisms," finding that "a cap will encourage carriers to operate more efficiently by limiting the amount of support they receive" and minimizing difficulties for rural carriers in adjusting to FLEC-based USF support. Indeed, as the Commission noted (para. 302), from its experience with the indexed cap on the existing HCF, the cap "effectively limits the overall growth of the fund, while protecting individual carriers from experiencing extreme reductions in support" (citations omitted).[13]

Fidelity (at 4) and USTA (at 10-11) contend that the Commission should have allowed a transition before limiting the amount of corporate operations expense that a carrier may recover from the USF to 115 percent of an amount projected for a service area of its size (para. 307). To the contrary, the Commission properly found (para. 283) that corporate operations expenses "not directly related to the provision of subscriber loops are not necessary for the provision of universal service" but "rather result from managerial priorities and discretionary spending." As such, the Commission was generous in allowing USF support for these types of expenses.

Finally, contrary to USTA's (at 8) and Western Alliance's (at 12) assertions, the Commission's decision (para. 308) to limit the amount of USF support for exchanges sold after May 7, 1997 at the same per-line support received by the seller is reasonable. It avoids the higher embedded cost-based subsidies available to rural ILECs from becoming a motivating

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[13] The successful operation of the cap is attested to by the fact that HCF recipients who experience significant adverse impact per loop per month were encouraged to submit waiver requests, yet it appears no waiver requests specifically directed at obtaining relief from harm caused by the cap on the HCF have been filed since the inception of the cap. See Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, Report and Order, 9 FCC Rcd. 303, para. 23 (1993). The waiver process remains open to any party that considers itself to be significantly harmed as a result of the cap.

factor in acquiring exchanges from lower cost companies, until all ILECs receive USF support based on FLEC.

III. THE COMMISSION SHOULD ADOPT A MANDATORY END USER SURCHARGE ON ALL INTERSTATE RETAIL TELECOMMUNICATIONS REVENUES AS THE RECOVERY MECHANISM FOR UNIVERSAL SERVICE SUPPORT.

Section 254(b)(4) of the Telecommunications Act of 1996 requires that all telecommunications service providers make an equitable and nondiscriminatory contribution to universal service support.[14] As AT&T showed in its Petition (at 1-7), the Commission's current USF recovery mechanism does not comply with this directive and should be reconsidered because it inappropriately transfers the ILECs' USF obligation to other carriers and, most fundamentally, it has an acute discriminatory impact on carriers who enter the local service market through total service resale ("TSR") and who have no ability to deflect their USF obligations to wholesale customers through access charges.

Like AT&T, MCI (at 7-8) recognizes that because of the operations of the Common Line formula, LECs will not be required to raise subscriber line charges ("SLCs") to reflect their USF assessment, which will instead be borne by interexchange carriers ("IXCs") through carrier access charges. As MCI (at 7) correctly points out, the Commission's rationale

[14] Although the Commission requires that USF support be *assessed* in a competitively neutral manner, *i.e.*, based on an interstate carrier's retail end user telecommunications service revenues (para. 772), the *recovery* of this assessment is not competitively neutral.

that this treatment is somehow necessary to avoid rate increases to consumers via the SLC is incorrect, because this treatment will only transfer from ILECs to IXCs the same pressure to impose end user charges.

Moreover, confirming AT&T's analysis, Comcast/Vanguard (at iv, 13) observes that unless the Commission orders a mandatory end user surcharge, CMRS and other competitive providers will be competitively disadvantaged because, while an ILEC can absorb double digit USF assessments that it can pass on to others through access charges, CMRS providers (like CLECs entering through TSR) will have to pass on the assessment to end users. Further, allowing ILECs "to mask their contributions and to recover them from the Carrier Common Line basket . . . perpetuates the practice of implicit subsidies" (U S WEST at 9-10) and conflicts head-on with Section 254(b)'s requirements. Accordingly, the USF recovery scheme adopted by the Commission is not competitively neutral and it should be replaced with a mandatory end user surcharge on all interstate retail telecommunications revenues.

Not only would a mandatory end user surcharge ensure competitive neutrality, it would also serve to address numerous other concerns raised by the parties. For example, it would moot the issue of whether the ILECs' USF assessments should be subject to price cap reductions through the normal operation of the X-Factor (productivity offset) in the price cap formula, an issue USTA raised in its Access Reform, CC Docket No. 96-262, Reconsideration Petition (at 5). And, as the Comcast/Vanguard (at iv, 13) confirm, it would also moot allegations by customers that a permissive pass-through of the USF support assessment somehow constitutes an abrogation of fixed-price contracts between carriers and their customers. Ad Hoc at 2-10; API at 3-5.[15] "Moreover, assessing contributions as a surcharge would also obviate the need for carriers to change their access [or end user] rates as a result of fluctuations in their support obligations." U S WEST at 10.

For these reasons and given the strong support for a mandatory end user surcharge (AT&T at 6 n.8, citing others; *see also* para. 853 n.2135), the Commission should reconsider the mechanism for recovering USF support and should adopt an explicit, mandatory end user surcharge on all interstate retail telecommunications service revenues "that is both based on and reflected in the end user's retail bill." U S WEST at 10.

With a mandatory end user surcharge, USF recovery would be explicit and the competitive neutrality problem would not arise because the *assessment* and *recovery* for USF support

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[15] AT&T strongly disagrees with Ad Hoc (at 2-10) and API (at 3-5) that the Commission has allowed carriers to abrogate customer contracts. Rather, the FCC has considered the issue and allowed carriers to flowthrough a specific cost to the end user (paras. 829, 851). Particularly because the rates in many customer contracts may already anticipate access reductions, it was eminently reasonable for the Commission to create a limited exception to the normal doctrine that a carrier may not typically adjust rates in such a contract. In all events, what the vociferous customer response here suggests is that the Commission may need to reduce the overall size of USF support to maintain strong public support for its programs.

would focus on retail end user revenues.[16] Under a mandatory end user surcharge, there would be no possibility whatsoever that access customers would bear the burden of the ILECs' USF obligation (whereas CLECs providing service through TSR would have no ability to deflect their USF obligation through access charges) because each carrier's USF obligation would be directly transferred to its end user customers.[17]

The Commission's sole basis for rejecting a mandatory end user surcharge was that it would "eliminate carriers' pricing flexibility to the detriment of consumers" (para. 853). To the contrary, because a mandatory end user surcharge is the most competitively neutral recovery mechanism, it will ensure that each consumer pays his or her fair share of universal service support.

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[16] Unlike for high cost/low-income support, USF support for schools, libraries and rural health care providers is assessed on both interstate and intrastate revenues (para. 772). However, the Commission decided to forego preempting state ratemaking authority by recovering all USF obligations, including that which is assessed on intrastate services, from interstate end user services. Universal Service Order, paras. 772-773, 807-809, 837. Although recovering this entire obligation from an end user surcharge on interstate services does not violate the competitive neutrality requirement, for the reasons discussed in Part I with respect to high cost support, a unified federal fund assessed and recovered from intrastate revenues as well would offer substantial benefits.

[17] If the Commission does not adopt a mandatory end user surcharge for USF recovery in this proceeding, it should, at a minimum in the Access Reform proceeding, allow the ILEC flow-back that is assigned to the Common Line basket to be recovered from end users via the SLC to the extent that actual SLC rates in a study area are below the SLC caps. See Access Reform Order, para. 174; see AT&T at 7 n.12; MCI at 7-8.

IV. THE COMMISSION'S INTERPRETATION OF SECTION 214(e) AS TO CERTIFICATION OF CARRIERS ELIGIBLE FOR UNIVERSAL SERVICE SUPPORT IS CORRECT AND NEED NOT BE FURTHER CLARIFIED OR RECONSIDERED.

In construing Section 214(e) as to which carriers may be certified as eligible for universal service support, the Commission found that: (1) neither it nor a state commission has discretion to deny USF eligibility status to a carrier seeking entry in nonrural LEC territories that meets the statutory criteria (paras. 24, 135-136); (2) a carrier using unbundled network elements ("UNEs") meets Section 214(e)(1)(A)'s requirement that it is providing the supported service "either using its own facilities or a combination of its own facilities and resale of another carrier's services" (paras. 24, 128, 151-180); and (3) service areas should not be unreasonably large, otherwise they would constitute barriers to entry (paras. 25, 129, 184-185; 186-190). For the reasons stated in the Universal Service Order, the Commission's above interpretations appear to be correct and will ensure that universal service support is made available consistent with the Act's overriding objective of "opening all telecommunications markets to competition."[18]

Although not disputing the merits of the Commission's findings, the Pennsylvania and Texas state commissions ask the FCC to clarify that its assertedly "overly prescriptive" (Texas at 9) pronouncements as to who shall be deemed to be an

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[18] See S. Conf. Rep. No. 104-230, 104 Cong. 2d Sess. 1 (1996).

"eligible carrier" for purposes of receipt of USF funding are "instructive rather than binding" (Pennsylvania at 2), given that Section 214 specifies that state commissions are to certify carrier eligibility status. Similarly, Florida (at 1) asserts that the "FCC has clearly overstepped its authority." Contrary to the state commissions' request, there is no need at this juncture for the Commission to announce whether this construction of the Act is deemed binding or precatory. Should a state certification decision reach a result that is inconsistent with the FCC parameters, a carrier can raise the issue at that time. In any event, if a state certification decision acts as a barrier to entry, because it is not competitively or technologically neutral, the FCC has express authority to preempt such a decision under Section 253(d) of the Act.

RTC (at 13-14, 17) and Western Alliance (at 23) erroneously contend that carriers providing service using unbundled network elements do not meet the "own facilities" requirement of Section 214(e). Without repeating the FCC's cogent rationale (paras. 151-180) as to why use of UNEs fulfills the statutory criteria, the principle of Section 214(e) is that the carrier that provides the supported service to subscribers in the service area is entitled to the subsidy. UNEs are a way that a competitive carrier can provide the supported service, and the UNE purchaser compensates the ILEC at the forward-looking economic cost of the facility (paras. 160, 162, 167). Therefore, to the extent that the forward-